

Chapter 70 Working Group Report

The Chapter 70 working group was formed pursuant to section 607 of the FY04 budget, with a charge as follows:

There shall be a house and senate working group to develop legislation to reform chapter 70 of the General Laws. The working group shall be made up of the president of the senate or his designee, the speaker of the house or his designee, the senate and house chairs of the joint committee on education, arts, and humanities, the chairs of the senate and house committees on ways and means and the minority leaders of the senate and house, or their designees. The working group shall address matters including but not limited to aid and required local contributions determined under chapter 70 and shall consider how best to allocate state funds equitably to cities, towns, and regional school districts. The working groups shall consider the appropriate balance of property value and income measures in setting local spending requirements, and shall recommend ways to reduce arbitrary discrepancies in required local contributions and state aid levels of similar districts. The working group shall draw on the expertise of interested parties including but not limited to representatives of the department of education and organizations representing educators, school administrators, and local officials. The working group shall submit preliminary recommendations to the joint committee on education, arts, and humanities on or before December 12, 2003.¹

Throughout the fall, members of the working group and their staff have met to discuss education funding reform. A hearing at the State House on October 22 gathered public input. The working group submits this preliminary report to inform members of the Legislature and the interested public of the substance of the working group's discussions and areas of developing consensus on guidelines for Chapter 70 reform.

Educators, municipal and state elected officials, and other advocates for education and for taxpayer equity have advanced countless proposals on education funding in recent years.² Many of these proposals share a belief that Chapter 70 aid should allocate similar aid to similar communities with similar enrollments and demographics, while reducing arbitrary discrepancies in local required spending amounts – although when the time comes to define “similar” and to grapple with the spending limits effectively imposed by Proposition 2 ½, that consensus becomes less firm. The working group's report on these issues reflect both the consensus over goals and the uncertainty over details that have been present in the debates of the past few years.

The working group broadly agrees that communities of similar fiscal strength should receive similar aid and have similar spending requirements. The working group is still struggling with defining a municipality's resources, choosing a defensible formula which would link the municipality's resources with a guaranteed aid level, and detailing and implementing the goals of a fairer, more rational system for distributing aid to districts. In many ways, the group has discovered that over the past several years, significant consensus has been reached on overall goals for chapter 70 reform, but very little consensus has been attained about the technical and statistical measures to be used in any transition, in part because discussions and testimony have not had the specificity necessary to produce a detailed consensus proposal. The group hopes to rectify that through its call in this document for more specific input on these measures in order to draft reform legislation.

The working group is also keenly aware of the state's fiscal challenges. Budget constraints leave little hope for significantly increased education funding in the near future. Thus the working group intends first

¹ Section 607 of chapter 26 of the acts of 2003, as amended by section 104 of chapter 140 of the acts of 2003.

² The working group reviewed the many recommendations for Chapter 70 reform which have been offered to the Education Committee and the Committees on Ways and Means in recent years. This report draws on those recommendations as well as on testimony offered at the October 22, 2003 hearing and on proposed legislation.

to lay out a framework for how greater equity might be brought to the calculation of local contributions, and how aid might be more progressively and fairly allocated in an enrollment sensitive manner to districts with net school spending above the foundation budget level. Reaching a fairer, more rational distribution of aid is a transition requiring controversial discussions of overall funding levels and measurement of communities' resources and abilities to pay.

Members of the working group are deeply committed to addressing inequities in Chapter 70 aid and local spending requirements. In light of the current fiscal challenges, some of the issues which have been identified by and to the working group will not be resolved in the FY05 budget, but it is our hope that this report helps build the parameters for reform. In addition, we hope to advance the dialogue on the statistical and technical details necessary for reform. The working group welcomes feedback on this report.

This report identifies areas in which the working group is particularly interested in opinions on the advisability and technical feasibility of changes to the formula. The working group asks the Education Committee to use this report and the discussion it engenders in its development of any future finance reform legislation. The working group requests that comments be directed to the Joint Committee on Education, Arts and Humanities (Room 473G, State House, Boston, MA 02133) or emailed to ssmith@senate.state.ma.us and kathleen.devlin@hou.state.ma.us by January 15, 2004.

Foundation Budget

The foundation budget is the state's legal calculation of the cost of running any school district, given its particular enrollment and demographics. Assuring that state aid gets all districts to foundation, regardless of local resources, is the core of Education Reform.

The foundation budget and the state's commitment to assure that the sum of local and state spending in every district is at or above foundation is at the center of Chapter 70. In light of the working group's primary mandate, however, and also in recognition that the Superior Court is currently reviewing the adequacy of the foundation budget in the *Hancock* case, the working group has not addressed the definition of the foundation budget.

Local Spending Requirements

Through Chapter 70, the state mandates a minimum amount that each city and town must appropriate for its schools. Spending requirements vary by community and are intended to reflect the state's estimate of local ability to pay.

- **Goal:** To rationalize local spending requirements in relation to communities' abilities to pay and to set similar spending levels so that similar communities have similar tax rates for educational purposes.
- **Issues Discussed by Working Group:**

Equity in Local Spending Requirements and Implicit Tax Rates

The major issue regarding local spending requirements is ensuring that the state's requirements for each community corresponds fairly with that community's ability to pay. The method of determining which communities have relatively high and low spending requirements is vital to

the process of narrowing the range of spending requirements for similar communities. The working group searched for a framework for comparing communities' spending requirements in a way that properly accounts for wealth and income levels. The implicit tax rates that would result from such a framework could be used to create more uniform local spending requirements.³ The methods discussed as possible ways to calculate implicit tax rates were:

- Calculating implicit tax rates using non-adjusted equalized valuations as determined by the state Department of Revenue.
- Adjusting required spending per \$1,000 EQV⁴ by median income as a percentage of state average.
- Applying an income adjustment only to residential properties and not adjusting commercial properties.
- Adjusting property values downward for communities of below average income but not making income adjustments to communities of above average income.
- Applying the downward-only method only to residential properties only.

Once the best adjustment factor is determined, the goal would be to bring every community's implicit tax rate to within a certain range over a period of time. This would moderate both the very high and the very low spending requirements and ensure that communities of similar fiscal strength had spending requirements within a defined range, as measured by their tax rates. The question of how to require increased spending in historically low effort communities is problematic, particularly in light of Proposition 2 ½ limits which fix in place low and high tax rates alike.

Net School Spending

Also discussed was limiting required net school spending amount to a percentage of the foundation such as 110% to 125% of foundation. Communities wanting to spend more would be free to do so, but the state could not require any school district to exceed the maximum. This approach would allow wealthy communities to maintain tax rates below the usual range if they were able to generate the revenue needed to meet their required net school spending at these tax rates.

The working group is aware that introducing a ceiling on local spending requirements and limiting required net school spending would allow for decreases in spending in some districts. For example, a town which currently has a required school spending of \$16,000,000 on a taxable base (adjusted for income) of \$1,000,000,000 in property, for a rate of \$16.00 per \$1,000 adjusted EQV, might be permitted to reduce its required local contribution if the state average rate were well below that \$16.00 rate. If the local district had required net school spending of 130% of foundation even after the rate reduction, the district required spending could be reduced further. Aid would not necessarily be increased to offset the reduction.

³ Implicit tax rates provide a basis for comparing spending requirements across the state. Implicit tax rates are calculated by dividing the required local spending by the tax base, possibly with an adjustment for income. For example, if a town has \$100 million in taxable property and the state requires that town raise \$800,000 for its schools, the implicit tax rate is \$8.00 per \$1,000 in property value because it must spend \$8 for every \$1,000 in taxable property. Further adjustments to taxable property for income levels can make the comparison more valid to other towns of similar property wealth but higher or lower income.

⁴ Equalized valuation, or EQV, is the total taxable property value in any city or town, calculated by the Division of Local Services at the Department of Revenue to allow comparison between municipalities at different phases in their three-year assessment cycle.

Whether to continue or eliminate an excess debt provision is also being considered. The excess debt allowance in current law allows above foundation communities who have higher than average capital costs per student to reduce their net school spending by that amount, provided spending does not drop below foundation.

- **Proposals for Adjusting Local Spending Requirements:**

While broad agreement exists among the working group that rationalizing local contribution requirements is important, no final decision was reached about what exact measures should be used. The following are measures the group found appealing:

- Retain a system of local spending based primarily on maintenance of prior year effort, but work to reduce spending requirements for the cities and towns with the highest tax rates for schools and to raise requirements for the cities and towns with the lowest tax rates for schools.⁵
- Identify the extent of variation in local spending requirements through the determination of an implicit tax rate for every community (required spending per \$1,000 EQV, adjusted in some manner by median income per taxpayer). The goal would then be to bring in both low effort and high effort outliers into a finite band of implicit tax rates.
 - *For example, if the state average implicit tax rate were \$10.00 per \$1,000 EQV, over a period of time, communities well above or well below would adjust their local spending to be within a defined range, such as \$7.50 to \$12.50. Required local contributions would be the product of local adjusted EQV and a rate within this band.*
 - *Over time, this band of implicit tax rates could be narrowed as the state's fiscal condition and Proposition 2 ½ constraints allow. The initial effort, however, would focus initial and meaningful contribution relief on the communities with the most egregiously excessive contributions rather than providing modest to negligible relief on every community even slightly above state average.*
- For the purpose of comparing implicit tax rates, the working group looks favorably at a “downward only” income adjustment, in which lower than average income would be used to adjust downward the available tax base, but no adjustment would be made to the EQV of towns with income above the state average.
 - *By using the “downward only” method, the state would not underestimate the tax rates of wealthy communities with median incomes above state average. At the same time, communities with below average income would have this constraint on ability to pay taken into account when determining their required local contribution. In this manner, a low income city's spending requirements could be relaxed in light of low income without exaggerating the property wealth of a high income town.*
- The working group is inclined to support an approach which does not distinguish between residential and commercial property when comparing the tax bases of cities and towns.

⁵ Maintenance of prior year effort under present practice means that required local contribution generally grows at the same rate as the municipal budget as a whole, as estimated by the municipal revenue growth factor (MRGF). The intent is to require that a municipality spend the same proportion of its budget on education as in prior years. MRGF incorporates estimates of growth in non-school state aid, property taxes as limited by Proposition 2 ½, and other revenues such as fees, fines, interest earnings, etc.

- **Areas for Comment:**

- What rate of growth in required local contribution should the state impose on very low spending cities and towns? How should the limits of Proposition 2 ½ be taken into account?
- To what extent should the state allow very high spending towns to reduce local contributions? Should every town above the state average be considered high spending or only those above a certain percentage of the state average?
- What, if anything, is a reasonable limit on required net school spending as a percent of foundation? 110%? 125%? Higher or lower?
- Is the “downward only” income adjustment described above advisable? Is the current measure of residually adjusted EQVs more understandable or accurate?
- Should there be adjustments to required local contribution for excess debt as under present law, or in some other manner?
- Is the municipal revenue growth factor (MRGF) an accurate representation of municipal revenue growth? If not, how should it be altered?

State Aid

Chapter 70 organizes the distribution of over \$3 billion in state funds to cities and towns. Aid levels are not less than the difference between the local foundation budget and local required spending. Aid amounts are also influenced by variable spending requirements and historical patterns of aid distribution.

- **Goal:** To maintain districts at foundation while attempting, as much as possible, to provide those districts which are of similar wealth and income levels and are spending at or above foundation with similar aid as a proportion of their foundation budgets.
- **Issues Discussed by Working Group:** The basic structure of Chapter 70 is to calculate the foundation budget, set local required spending levels, then allocate state aid, which must be at least enough to get all districts’ net school spending (state plus local funds) to the level of foundation. The working group supports this general structure, but recognizes the concerns of districts that receive dramatically different shares of their foundation budgets as aid as a result of the formula’s reliance on historic aid levels, its lack of responsiveness to enrollment change, and the “hold harmless” aid, which collectively undermine rational distribution of aid.

A major technical concern in distributing aid in an equitable manner is the method used by the state to assess local fiscal strength. Discussion has centered on what factors and methods should be used to best reflect a community’s fiscal capacity. The following possibilities were considered:

- Use only equalized property value (EQV). The rationale for this method is that the amount of revenue a town can generate, regardless of its income level, is determined primarily by its property taxes; therefore property values most accurately indicate a town’s tax base.
- Use a combined measure of property wealth and income. If setting local contribution requirements in strict proportion to taxable property value helps standardize tax rates, it also can overstate the extent to which residents can access wealth tied up property when they are paying their taxes. This can be a particular problem for residents whose properties have appreciated dramatically in value while their income has changed little.

- If an income adjustment is deemed appropriate, a choice must be made about the relative merits of using median versus average income. Average income is a measure which makes a town look excessively wealthy as a result of a single high income household, or a handful of such households, which median income avoids. Note that the data sources are different, with average income data most readily available from the U.S. Census every ten years, while median income data is available from the Department of Revenue, but only for those who are required to file income taxes.
- One way of adjusting wealth for income is simple multiplication. For example, if a town's income as a percent of the state median income were 82%, then its equalized valuation would be multiplied by 82%, with that total compared to the state average. An alternative method is to average wealth and income such that a town with wealth at 95% of the state average and income at 85% of the state median would have a fiscal strength of 90% of state average.
- A third issue that must be addressed is whether the final judgment of wealth should be based on wealth per student, a better reflection of the town's ability to pay specifically for education, or wealth per resident, potentially a better reflection of public intuitions about which towns are wealthier or poorer.
- Finally, any income adjustment can be made to all property, or alternatively, only residential property. Income is of direct relevance to residential property owners, but local businesses are also affected by local income levels. Failing to adjust for non-residential property for income in above average income towns wrongly gives the impression that towns with some commercial tax base have less capacity to tax than those with entirely residential property.

While there has been no resolution on this matter, discussion centered on adding what has been called a "target share" approach to determining how much state aid a district receives, provided that every district is first guaranteed enough aid for spending to be not less than foundation. In order to establish a basis for comparing aid to similar communities, the state could create a sliding scale linking fiscal strength to levels of state aid as a percentage of foundation budget. For example, any town with average fiscal strength would receive a fixed percentage of its foundation budget in state aid, while a relatively better off town might receive a lower percentage.

Even if a common definition of local resources can be agreed upon, significant decisions must be made about how to translate those wealth levels into guaranteed levels, and about what mathematical formula should be used in that endeavor. Here the working group did not reach final resolutions, as significant questions are presented by the attempt to define this formula:

- A formula may be written so that towns of greater wealth get steadily and proportionally less aid as a percent of foundation. Graphically, this is represented as a line, and tends to be very expensive. (figure 1 below)
- A formula may be written corresponding to a curve. Even at this point, choices are infinite. A curve can be drawn in such a manner as to give the poorest towns sharp increases in percentages of guaranteed aid or to give dramatic increases to wealthy towns currently receiving very low aid percentages (figure 2 below). Drawing such a curve requires technical decisions about what percentage an average community should receive, what slope the line should have above and below that point, and how much is available to fund any such formula.
- The formula can be written to generate a wide variety of costs. Target share curves can be drawn so high that almost every district receives more aid, which is prohibitively

expensive for the state, or so low that no district requires more aid, which makes the proposal undesirable to districts. (figure 3 below)

- Finally, if a curve is drawn in the middle of the present distribution, legislators face yet another set of decisions. One choice is to use the curve only for aid increases for districts presently below the curve and not for aid cuts for those above. This makes any target share proposal more expensive. The second choice is to bring every district receiving less than its share up to targeted levels of funding while reducing the aid of any district receiving more than its share. This makes a formula with generally higher target shares less expensive, as allowing reductions helps make the whole formula revision more cost neutral.

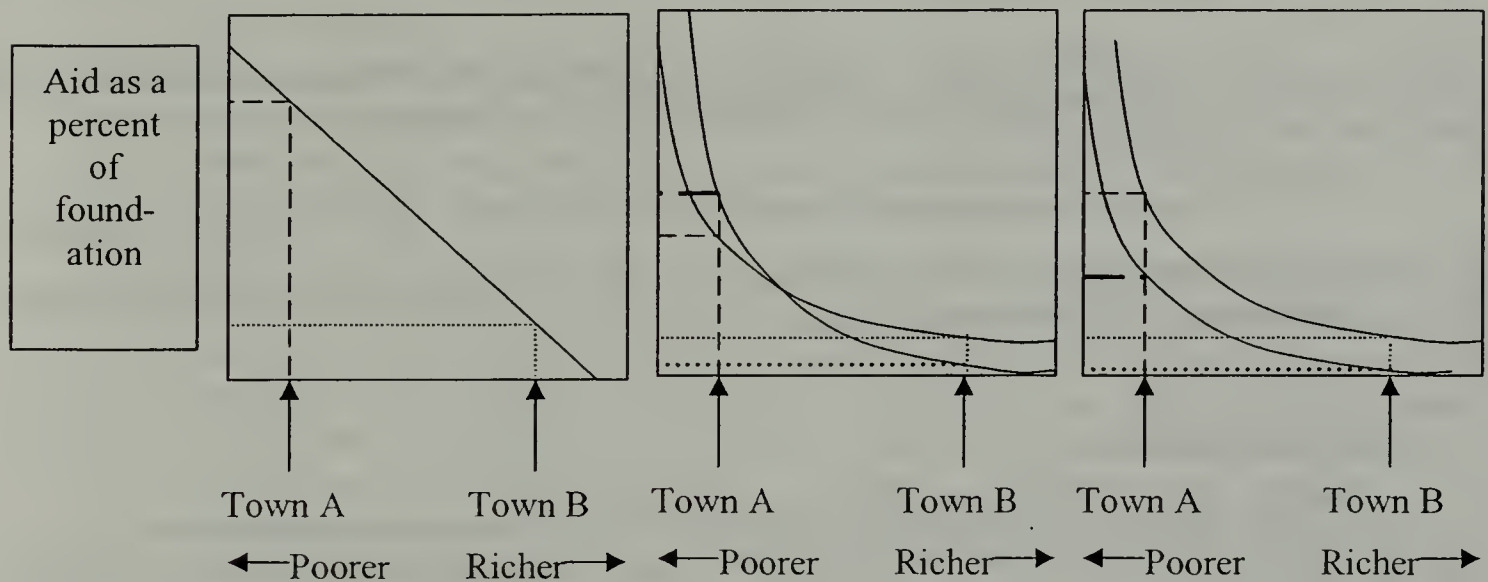


Figure 1

Figure 2

Figure 3

A subsidiary but important part of the group's discussion was the possibility of establishing both a floor and a cap on how much aid each districts receives as a percent of foundation. In the first instance, each district would be guaranteed aid in the amount of 10-15% of its foundation budget. On the positive side, this is a simple, easy to explain proposal that addresses the considerable concerns of those districts most aggrieved at the low levels of support they currently receive. On the negative side, it directs money at the very wealthiest districts in the state.

The second proposal was to establish a cap on how much aid a district can receive as a percent of foundation. Non-operating districts, in particular, often receive aid well in excess of 100% of foundation as a result of aid being held harmless despite dramatic reductions in the number of students served, and even, in some instances, the loss of every student previously being served by the non-operating district.

• **Proposals for Aid Distribution:**

The working group supports maintaining foundation aid as the core of Chapter 70, while attempting, as much as possible, to rationalize the distribution of aid.

- Keep spending in all districts at least at foundation should remain the state's top priority.
 - *The primary determinant of state aid for many communities would remain the amount necessary to fill the gap between foundation and required local spending.*

- An approach which over time directs similar aid to similar communities would improve the present distribution.

While broad agreement exists among the working group that such an approach represents an important step in rationalizing state aid to above foundation districts, no final decision was reached about what exact measures of wealth should be used, nor the exact formula used to calculate the resultant aid. The following are measures the group found most appealing:

- Use an average of income and EQV (as opposed to a product of the two) to compare local fiscal strengths.
- Use median income per capita when determining income (as opposed to average income per capita).
- Treat residential and commercial EQV in the same manner when assessing wealth (as opposed to applying an income adjustment to residential but not commercial property).
- Use EQV per resident when determining wealth (as opposed to EQV per pupil).
- The working group looks favorably on a floor and a ceiling for aid to any district at some percentage of the foundation budget.

- **Areas for Comment:**

- Should the state directly link aid levels to local resources, with the aim that similar communities be allocated aid equal to the same percentages of their foundation budgets? How?
- When comparing districts' local fiscal strength, should wealth be measured per pupil or per resident, and why?
- Is median (as opposed to average) the best measure of local income?
- What should be the formula for (i.e. the shape of) any sliding scale tying aid to local resources? What share of foundation budgets should an average wealth district receive as aid? What should be the slope of the curve above and below that point?
- For the purpose of drawing a sliding scale, what are the profiles of communities most in need of more aid? (E.g. should new aid go to communities receiving the lowest percentages of the foundation budget from the state, even if many of these communities have strong local tax bases? Or to communities of below average wealth and income, even if those communities have receive the greatest share of state aid in the past?)
- Should a sliding scale approach be used to implement cuts to districts above the target share curve? If not, what is the fairest basis for reductions in aid if such reductions are needed to balance the state budget or increase distributions to historically underfunded districts?

Regional Schools

The state specifically mandates that a town appropriate no less than a given amount to support regional school districts of which that town is a member. The state also allocates aid directly to regional schools.

- **Goal:** To make the state's requirements for regional school assessments reasonable and fair for both member municipalities and regional districts.

- **Issues Discussed by Working Group:** The working group acknowledges that regional spending requirements allocate local dollars to regional schools in a manner reflecting history more than regional needs or local obligations. State aid has offset regional spending irregularities to some extent – but, as a result, has also incorporated some of the variability of spending requirements. The group discussed the following points:
 - The current system for setting regional spending requirements is unresponsive to enrollment changes, and unrelated to the enrollment shares of each member of the region, which prior to 1994 defined each members' contribution under regional agreements. As a result, different members of the same regional face very different per student required spending amounts.
 - The variability is particularly wide for members of some vocational districts because of the large swings in percent terms from year to year in the number of students any given town sends to its vocational district. It may be preferable to set local spending requirements for vocational districts on a per-student basis.
 - The allocation of a municipality's contribution to the districts is not directly related either to the share of the municipality's students who attend that district, nor to the share of the town's overall foundation budget represented by that district. Although modest steps have been made in recent years to use foundation share as the basis for allocation, they have not uniformly remedied the problem, and, in some cases, may never do so. Because contribution levels drive aid decisions, misallocating contribution automatically misallocates aid, providing excessive foundation aid to districts receiving too little of the town's required contribution, while a district receiving too much of the town's required contribution may never be judged in need of aid. Thus, regional aid and spending requirements in many cases create dramatically different state/local shares for the different districts of which a town is a member – one town may pay 30% of the foundation budget of its local district, and much more or much less of the foundation budget associated with its students attending regional academic and vocational districts.
 - Some of the discrepancies in spending requirements and aid can be reduced by swapping state and local money on paper such that a town gets from the state as near as possible the same percent of the foundation budgets associated with its students at each of the districts of which it is a member. Where aid is shifted from a local to a regional district, local dollars can be shifted from the regional to the local district to fully net out the impact on required net school spending for both districts.
- **Proposals for Addressing Regional Issues:** The working group has had only preliminary discussions of what changes could and should be made to how the state sets spending requirements for and allocates aid to regional school districts. More information is needed on this subject, and the working group is particularly interested in comments from regional school districts and their members on regional issues.
 - The working group has an interest in smoothing historical discrepancies in aid and spending requirements as much as possible. The working group looks favorably on the “zero-sum shift” outlined in the Foundation Budget Review Commission report from 2001.

- **Areas for Comment:**

- Are there technical or other impediments to swapping local and state dollars on paper via a “zero sum shift” in order to even out differences in aid allocated to the various districts of which a town is a member? What is the appropriate way to allocate regional district aid to member towns when assessing what proportion of the foundation budget consists of state aid for each district of which a town is a member?
- Whether or not a zero-sum shift is used to iron out variations in aid on a one-time basis, what is the best way in the future to allocate required local spending to regional districts such that discrepancies between a town’s contributions to each of its districts do not widen over time?
- Should the state attempt to calculate the foundation budget associated with each sending town by incorporating that sending town’s actual students (low income, bilingual, etc) rather than pro-rating the foundation budget according to a town’s share of total enrollment?
- Is it advisable to treat vocational districts differently from all other districts in setting required contributions at a uniform amount per student for all sending districts? Is there a better alternative?
- Does it make sense to set required contributions for vocational districts on a per student basis, perhaps using a three year running average of enrollment? Should the per student amount be set at a uniform rate for all sending municipalities of any given vocational district? If not, how should per student required spending be adjusted to account for differences in ability to pay of sending cities and towns?
- Should spending requirements for regional academic and/or vocational school districts be linked to varying percentages of the foundation budgets associated with students from each sending town such that towns’ spending requirements are more directly linked to ability to pay?

MEMBERS OF THE WORKING GROUP

The Honorable Robert A. Antonioni,
Chair, Joint Committee on Education, Arts, and Humanities

The Honorable Marie P. St. Fleur,
Chair, Joint Committee on Education, Arts, and Humanities

The Honorable Joan M. Menard,
Designee of the Senate President

The Honorable Peter J. Larkin,
Designee of the House Speaker

The Honorable Therese Murray
Chair, Senate Committee on Ways and Means

The Honorable John H. Rogers
Chair, House Committee on Ways and Means

The Honorable Jo Ann Sprague
Designee of the Senate Minority Leader

The Honorable Paul J. Loscocco
Designee of the House Minority Leader

